

***THE RETIREE DRUG SUBSIDY:
MORE SECURE COVERAGE FOR RETIREES***

The Medicare Modernization Act (MMA) contains new retiree drug subsidies designed to encourage employers and unions to continue providing high quality prescription drug coverage for their retirees. This alternative retiree drug subsidy provides special tax-favored payments to qualified retiree prescription drug plans. The retiree drug subsidy program has highly flexible rules that permit employers and unions to continue providing drug coverage to their Medicare-eligible retirees while retaining their current plan designs that are at least equivalent to the standard Part D drug benefit, and using the retiree drug subsidy to reduce the cost of providing generous coverage. Sponsors of employer and union plans who offer a drug benefit as good as, or better than, Medicare's drug benefit will be able to apply for the subsidy, which is estimated to roughly average \$611 per beneficiary in 2006. Under our proposed policy, plan sponsors will have to incur costs at least equal to the amount they receive from Medicare – so no “windfalls” are available to employers or unions.

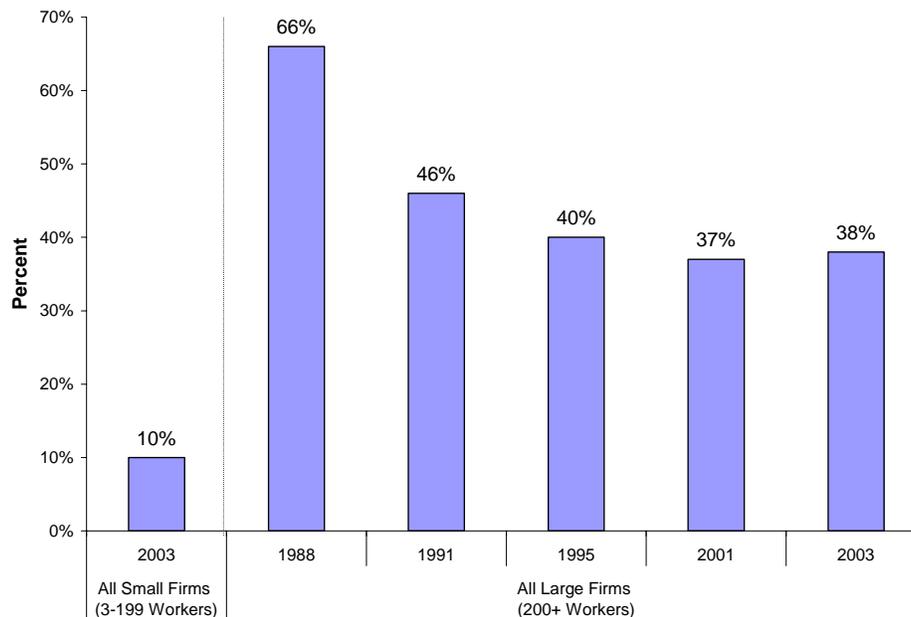
The Medicare Part D drug benefit also offers employers a variety of other options available to employers and unions to provide enhanced coverage to their Medicare retirees at a lower cost. They can choose to provide enhanced drug coverage to their Medicare-eligible retirees through, or in coordination with, Part D by encouraging their retirees to enroll in Part D (with Medicare subsidizing the costs of their standard Part D benefits), and providing enhanced coverage over and above the standard Part D benefit. This can be achieved by either providing separate supplemental drug coverage that wraps around a Part D plan (similar to policies that wrap around Medicare benefits under Part A and Part B), arranging for a Part D plan [that is, a prescription drug plan (PDP) or a Medicare Advantage Prescription Drug Plan (MA-PD)] to provide enhanced benefits to their retirees, or choosing to become a Part D plan that offers enhanced benefits to their retirees. In all of these cases, financial support from the new Medicare drug subsidy can augment contributions by employers to provide a more generous and less costly drug benefit for retirees than is possible through employer support alone.

The Medicare prescription drug benefit and retiree drug subsidy represent additional funding sources that can help employers and unions continue to provide high quality drug coverage for their retirees. We anticipate that this new funding will generally improve support for retiree drug coverage, enhancing both its quality and security.

Retiree coverage has been in decline for many years

Employer-sponsored retiree health insurance has been an important source of drug coverage for many Medicare beneficiaries. However, for well over a decade, the availability and generosity of employer-sponsored retiree health coverage has been eroding, particularly for future retirees. As prescription drug costs have risen, employers have been shifting more of those costs to their retirees, and many employers have ceased offering retiree health coverage altogether.

Percentage of Large Firms Offering Retiree Health Benefits, 1988-2003



Source: Kaiser/HRET Survey of Employer Sponsored Health Benefits: 2001, 2003; KPMG Survey of Employer-Sponsored Health Benefits: 1988, 1991, 1995. The denominator is all firms that offer health benefits to active workers.

In 1988, 66 percent of large employers that offered health benefits to active workers also offered retiree health benefits. In 2003, only 38 percent of large employers offered them. During the same year, only about 10 percent of small firms that offered health benefits to active workers also offered retiree health benefits. The picture is even starker for future retirees, who have been disproportionately affected by most of these changes.

Medicare is helping employers continue to provide retiree health care coverage

The new retiree drug subsidy will pay employers and unions to continue offering the prescription drug coverage they currently offer as Medicare's own benefit comes online. The proposed regulation reflects our four objectives of maximizing the number of retirees benefiting from the retiree drug subsidy, avoiding windfalls, minimizing administrative burden and not exceeding budget estimates. In doing so, we are considering a range of potential options discussed in the Preamble, each of which may have an impact on achieving the key objectives. We seek comments on how best to accomplish these goals, recognizing both that there may be tradeoffs, and that our implementation must be consistent with the statutory authority provided the Secretary.

The new law will pay a retiree drug subsidy to employers and unions that offer drug coverage that is as good as, or better, than Medicare's standard drug benefit. The subsidy will be available to a broad range of private and government employers, including city and county governments and church plans. The subsidy varies depending on how high their retiree drug costs are. It pays 28 percent of each qualifying enrollee's annual allowable drug costs between \$250 and \$5,000 in 2006. Moreover, the retiree drug subsidy amounts are tax-free, which increases their value to employers. The subsidy is estimated to roughly average \$611 per beneficiary in 2006.

Employers and beneficiaries will have multiple options for enhancing retiree coverage through new Medicare subsidies

To maximize the continuation of retiree coverage, CMS is proposing that the Medicare retiree drug subsidy be designed to be flexible enough to enable employers and unions to obtain the subsidy without disrupting their current coverage. Employers' options include:

- Continuing to offer retiree prescription drug coverage and accepting the new Medicare retiree drug subsidy. With this option, many employers can continue the same drug plans they offer today, uninterrupted, while receiving a substantial Federal subsidy to reduce their costs. Retirees can decline to enroll in the new standard Medicare drug benefit and remain in their employer or union plan, which may also offer better coverage.
- Supplementing the new Medicare drug benefit. Employers also have the option of declining the retiree drug subsidy and encouraging their retirees to enroll in Medicare's new prescription drug plans, or in Medicare Advantage plans that offer drug coverage, while opting to provide them with extra help. There are several ways that employers could supplement the standard Medicare drug benefit:
 - They may pay for supplemental coverage through an enhanced Medicare plan that fills in more of the cost-sharing;
 - They can set up their own external supplemental plans and coordinate benefits with the Medicare drug plans, providing extra help with cost sharing;
 - They may also choose to provide assistance with the basic drug premium for Medicare; and,
 - They can choose to set up special prescription drug plans, or Medicare Advantage plans, for their retirees. CMS plans to use its waiver authority to allow employers to make special arrangements with prescription drug plans and Medicare Advantage plans for their retirees. These waivers would allow employers and plans to provide more flexible benefits and to limit enrollment to the retiree population.

It is important to remember that retirees who choose to continue with their employer-sponsored drug coverage will always be able to enroll in the Medicare prescription drug program at a later date, free from any late enrollment penalties, as long as their employer's drug coverage is at least as generous as the standard Medicare drug benefit.

We are seeking comments from retirees, employers, unions and others on the best way to implement all of those options in order to reduce retiree drug costs.

Comments on the proposed regulations will be accepted until October 4, 2004. Comments should be submitted to the Centers for Medicare & Medicaid Services at www.cms.hhs.gov/regulations/ecomments